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THE SUPREME COURT'S CONSTRUCTION OF THE FEDERAL CONSTITUTION IN 1920-1921, II[1]

II. REGULATION OF COMMERCE

1. *Power of Congress*

IN a proceeding brought by the United States to restrain the construction of a dam in a stream alleged to be a "navigable river, or other navigable water of the United States," *Economy Light & Power Co.* v. *United States*[2] held that "a river having actual navigable capacity in its natural state and capable of carrying commerce among the states is within the power of Congress to preserve for future transportation, even though it be not at present used for such commerce, and be incapable of such use according to present methods, either by reason of changed conditions or because of artificial obstructions." Mr. Justice Pitney declared also that "the authority of Congress to prohibit added obstructions is not taken away by the fact that it has omitted to take action in previous cases." The river in question had once been used for navigation and was a continuous stretch of water from the Chicago Divide to its mouth. Such rapids and boulders as prevented navigation at the present time did not affect navigable capacity. Therefore, the construction of a dam was enjoined.[3]

[1] For the preceding instalment reviewing cases on Miscellaneous National powers, see 20 MICH. L. REV. 1.

[2] 256 U. S. —, 41 Sup. Ct. 409 (1921).

[3] The following articles deal to some extent with questions of federal power under the commerce clause: George Gleason Bogert, "Problems in

Turning from water to other liquids, we find *Williams* v. *United States*[4] reaffirming the constitutionality of the Reed Amendment by which Congress forbade the transportation in interstate commerce of intoxicating liquor into any state whose laws prohibited the manufacture or sale therein of intoxicating liquor for beverage purposes. Chief Justice White characterized as frivolous the objection that as the applicability of federal prohibition depends on the varying laws of various states the act was a violation of the constitutional provision prohibiting any regulation of commerce which gives a preference to the ports of one state over those of another.[5]

Cases in which the issue is the applicability of a federal statute to the situation before the court may in effect produce adjudications of the extent of federal power, even though technically the decision is confined to statutory construction. This is clearly so when the federal law is held applicable. If the parties do not think it worth while to raise a constitutional objection, the possible objections may be assumed to be pretty slim ones. Of the four cases involving the Sherman Law two found the alleged restraints of trade to be within the prohibitions of the statute. *United States* v. *Lehigh Valley R. Co.*[6] broke up a combination between an interstate railroad, a coal company and a sales company whereby the carrier controlled the interstate shipment through its control of production. The sales company was owned almost entirely by

Aviation Law," 6 CORNELL L. Q. 271; Walter L. Fisher, "The Packers and the Public," 15 ILL. L. REV. 504; Stanley B. Houck, "Jurisdiction and Procedure of the Federal Trade Commission," 15 ILL. L. Rev. 518; R. H. McRoberts, "The Growth of Federal Control Over Business Since the Establishment of the Interstate Commerce Commission," 6 VA. L. REG. n. s. 334; Max Schoetz, Jr., "Federal Control of Corporations," 5 MARQUETTE L. REV. 108; Henry Veeder, "The Federal Trade Commission and the Packers," 15 ILL. L. REV. 485.

[4] 255 U. S. —, 41 Sup. Ct. 364 (1921).

[5] The ante-Eighteenth Amendment federal regulations of intoxicating liquor under the commerce clause are treated in an anonymous article entitled "An Examination of Wilkerson v. Rahrer," 25 DICKINSON L. REV. 1, and in Noel T. Dowling and F. Morse Hubbard, "Divesting an Article of Its Interstate Character," 5 MINN. L. REV. 100, 253.

[6] 254 U. S. 255, 41 Sup. Ct. 104 (1920). See 19 MICH. L. REV. 553. Chief Justice White and Mr. Justice Holmes concurred only because of prior controlling decisions, and Justices McReynolds and Brandeis did not sit.

stockholders of the carrier and was entirely controlled by it, so that the transportation by the carrier of the products bought by the sales company was held to be within the prohibitions of the commodities clause of the Hepburn Act.[7] In *Duplex Printing Press Co.* v. *Deering*[8] an interference with plaintiff's interstate trade was accomplished by exerting pressure on customers in New York to refuse to buy the products of a Michigan factory. This interference was held to violate the Sherman Law. There was no contention that the commerce involved was not interstate, nor was such a contention advanced in the two cases[9] in which the acts complained of were held not to violate the Sherman Law.[10]

In two cases the validity of a stipulation limiting the liability of the carrier to a designated amount was held to be governed by

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[7] In 69 U. PA. L. REV. 66 is a note on the interpretation of the commodities clause. In 19 MICH. L. REV. 221 is a discussion of the application of the commodities clause in United States v. Reading Co., 253 U. S. 26, 40 Sup. Ct. 425 (1920).

[8] 254 U. S. 443, 41 Sup. Ct. 172 (1921). See 21 COLUM. L. REV. 258, 19 MICH. L. REV. 628, and 1 WIS. L. REV. 187. The defendants' acts in this case were clearly violations of the Sherman Law under previous decisions, and the issue was whether they were within a provision of the Clayton Act prohibiting injunctions against designated acts of employees in the course of a dispute over conditions of labor. The majority held that they were not and granted the injunction. Justices Brandeis, Holmes and Clarke dissented. In the course of the majority opinion Mr. Justice Pitney observed that the acts of Congress "are of paramount authority, and their prohibitions must be given full effect, irrespective of whether the things prohibited are lawful or unlawful at common law or under local statutes."

[9] Frey & Son v. Cudahy Packing Co., 256 U. S. —, 41 Sup. Ct. 451 (1921), and Geddes v. Anaconda Copper Mining Co., 254 U. S. 590, 41 Sup. Ct. 209 (1921). The latter case involved the sale of a mine to a competing company; the former had to do with the effort of a manufacturer to fix resale prices. There were no explicit contracts restricting the resale price, but the trial court had charged that from the facts recited the jury might reasonably infer an understanding. A majority of the court thought that the facts recited did not warrant the charge, though they recognized that "essential agreement, combination or conspiracy might be implied from a course of dealing or other circumstances." The dissenting judges, Justices Pitney, Day and Clarke, regarded the charge of the trial court as less directory than did the majority.

[10] For discussions of a case holding that contracts with regard to organized baseball are not interstate in character and so not within the Sherman law, see 34 HARV. L. REV. 559 and 19 MICH. L. REV. 867.

federal law. *Galveston, H. & S. A. Ry. Co.* v. *Woodbury*[11] involved the loss of a trunk checked between two Texas points on a ticket from Canada to Texas and return. Mr. Justice Brandeis said that the journey, if started in New York instead of Canada, "would have been interstate, although the particular stage of it on which the trunk was lost lay wholly within the state of Texas." The fact that the start and finish were in Canada rather than in the United States was material only to the question whether Congress had in fact undertaken to regulate such journeys. This question was answered in the affirmative.[12] In *Western Union Telegraph Co.* v. *Esteve Brothers Co.*[13] it was not contested that federal law is applicable to the liability for error in a cable message sent from Spain to the United States. The dispute was on the issue of what the federal rule actually was.[14]

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[11] 254 U. S. 357, 41 Sup. Ct. 114 (1920).

[12] The Act of 1887 declared that it applied to any common carrier engaged in transportation "from any place in the United States to an adjacent foreign country." Mr. Justice Brandeis observed that "a carrier engaged in transportation by rail *to* an adjacent foreign country is, at least ordinarily, engaged in transportation also *from* that country to the United States," and declared that "the test of the application of the act is not the direction of the movement, but the nature of the transportation as determined by the field of the carrier's operation."

The law of liability here applied was not one actually provided by Congress, but the common law known to the federal courts as distinguished from that known to state courts and in this instance as opposed to that known to the Texas courts. The idea of the federal courts is that a shipper who has availed himself of a lower rate conditioned on limitation of liability to a designated value is estopped to claim that the value is more than that when it was open to him to pay a higher rate for an unlimited liability. In this case the filing of the tariffs with the Interstate Commerce Commission was held enough to limit the liability when the tariff so provided in case the excess rate was not paid, even though the ticket bought by the passenger in Canada contained no notice of any limitation of liability and the passenger was not notified of any such limitation when he bought his ticket or when he checked the trunk between the two Texas points.

[13] 256 U. S. —, 41 Sup. Ct. 584 (1921).

[14] All the rates filed by the company were accompanied by stipulations limiting liability, but the limitation for repeated messages was higher than that for unrepeated ones. Mr. Justice Brandeis declared that "the fact that the alternative rate had tied to it a provision which, if tested, might be found to be void, is not material in a case where no effort was made to take advantage of it." Here again the court regarded its ideas of common law as a

United States v. *Northern Pacific Ry. Co.*[15] held the federal Safety Appliance Act applicable to two so-called transfer trains operated on a terminal railroad some four miles long. The issue was simply whether these trains were trains within the meaning of the statute. As to this, Mr. Justice Brandeis said:

> "A moving locomotive with cars attached is without the provision of the act only when it is not a *train;* as where the operation is that of switching, classifying and assembling cars within railroad yards for the purpose of making up trains."

Inasmuch as the Safety Appliance Act is held constitutionally applicable to all trains on tracks over which interstate trains run, without regard to the question whether the facilities in question are used for interstate commerce, it is reasonable to assume that Congress might, if it chose, prescribe the appliances of all cars and engines on such tracks.[16]

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part of the regulation provided by the federal statute. An interesting question is suggested by the statement of Mr. Justice Brandeis that where "the general public upon paying the rate for an unrepeated message accepted substantially the risk of error involved in transmitting the message, the company could not, without granting an undue preference or advantage, extend different treatment to the plaintiff here." Suppose suit for the error had been brought in Spain, where the message was sent, and judgment for the full loss had been recovered. Would the company by paying the judgment violate the federal statute against discrimination?

For a discussion of credit extension as an unfair practice under the Interstate Commerce Act, see 69 U. PA. L. REV. 365.

In Union Pacific R. Co. v. Burke, 255 U. S. 317, 41 Sup. Ct. 283 (1921), a carrier was held liable for the full value of the goods lost, since there was only one published rate and the shipper therefore had no choice of rates for a limited liability or rates for an unlimited one.

In New York Central & H. R. R. Co. v. York & Whitney Co., 256 U. S. —, 41 Sup. Ct. 509 (1921), commission merchants who were consignees of perishable products and who had paid all the demands of the carrier were held bound to pay more when the carrier discovered that it had by mistake charged less than the established rates. The consignees had no contracts with the carriers and they had already settled with the consignors on the basis of the charges originally made by the carrier.

[15] 254 U. S. 251, 41 Sup. Ct. 101 (1920).

[16] Lang v. New York Central R. Co., 255 U. S. —, 41 Sup. Ct. 381 (1921), in applying the rule that the Safety Appliance Act can be the foundation of

An effort to hold an initial carrier liable under the Carmack Amendment for loss on the line of a later carrier met with defeat in *Bracht* v. *San Antonio & A. P. R. Co.*[17] because the court found that the contract with the initial carrier was for an intrastate shipment only and that the later interstate shipment was a wholly new venture. There was at the outset no contemplation on the part of shipper or carrier that the goods would go beyond the destination named. The case was therefore distinguished from earlier ones in which the general course of business warranted the conclusion that the initial carriage on an intrastate bill of lading "was really but part of an interstate or foreign movement reasonably to be anticipated by the contracting parties—a recognized step towards a destination outside the state." The decision in the principal case was based on statutory construction, but it is plain that an effort by Congress to impose liability on the initial carrier under the circumstances here involved would encounter serious constitutional obstacles.[18]

2. *State Police Power and Interstate Commerce*

A provision in the state charter of an international bridge corporation requiring it to construct and maintain a roadway and pathway over its bridge was sustained in *International Bridge Co.* v.

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liability to injured employees only when the carrier's failure to comply with the act is the proximate cause of the injury, held that the absence of a coupler on a car was not the proximate cause of an injury suffered by a brakeman who was squeezed between the top of the defective car and the top of a moving car on which he was sitting, even though the presence of a coupler on the offending car would have kept the moving car from coming into such close proximity to it as to permit the squeezing which caused the injury. Justices Clarke and Day dissented.

[17] 254 U. S. 489, 41 Sup. Ct. 150 (1921).

[18] The power of Congress over intrastate rates is considered in Minor Bronough, "Federal Control of Intrastate Rates," 24 LAW NOTES 187, and in notes in 6 CORNELL L. Q. 412, 21 COLUM. L. REV. 352, and 69 U. PA. L. REV. 262.

In 69 U. PA. L. REV. 385 is a note on Wells, Fargo & Co. v. Taylor, 254 U. S. 175, 41 Sup. Ct. 93 (1920), holding that an express company is not a "common carrier by railroad" within the meaning of the federal Employers' Liability Law. Southern Pacific Co. v. Berkshire, 254 U. S. 415, 41 Sup. Ct. 162 (1921), which passes on questions of negligence and assumption of risk

New York[19] against the objection that it usurped the power of Congress over foreign commerce. The contention that Congress had assumed such control of the particular bridge as to exclude state intermeddling was also held to be unfounded. Congress had passed a statute requiring its consent to a bridge across international waters, but prior to this statute Congress had authorized this bridge and declared it to be a lawful post road. Mr. Justice Holmes observed that the mere fact that a bridge spans national boundaries does not deprive the state of control in the absence of congressional action, and that when Congress has acted there is no reason for not leaving the situation as Congress has seemed to leave it. The case evidently caused the Supreme Court some difficulty, for a decision was reached only after a reargument, and the Chief Justice and Justices McKenna and McReynolds dissented.[20]

Over the dissent of Justices Pitney and Clarke, *St. Louis & S.*

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under the Employers' Liability Law, is treated in 21 COLUM. L. REV. 389. In 69 U. PA. L. REV. 270 is a consideration of Director General of Railroads v. Viscose Co., 254 U. S. 498, 41 Sup. Ct. 151 (1921), which holds that action of a carrier in cancelling the published classification and rates on artificial silk and including such silk among the articles that will not be accepted for shipment is a change in classification and so a matter of which a shipper cannot complain in the courts in the absence of review by the Interstate Commerce Commission. Justices McKenna, Van Devanter, Pitney and McReynolds dissented.

In 15 ILL. L. REV. 284 is a consideration of Kansas City So. Ry. v. Interstate Commerce Commission, 252 U. S. 178, 40 Sup. Ct. 187 (1920), 19 MICH. L. REV. 26, which compelled the commission to estimate certain hypothetical costs which the court itself had declined to do on the ground that such estimation was "wholly beyond the reach of any process of rational determination."

Some problems of federal control of railroads are treated by Blewett Lee in "Consolidation of Carriers Under the Transportation Act, 1920," 6 A. B. A. JOUR. 185.

[19] 254 U. S. 126, 41 Sup. Ct. 56 (1920). See 16 ILL. L. REV. 130.

[20] Pennsylvania Gas Co. v. Public Service Commission, 252 U. S. 23, 40 Sup. Ct. 279 (1920), 19 MICH. L. REV. 29, which allowed a state to regulate the price of natural gas of extra-state origin, is discussed in 27 W. VA. L. Q. 180, 201. State regulation of the price of coal in the hands of the producers was held to be a regulation of interstate commerce in an Indiana case considered in 19 MICH. L. REV. 415. The question whether the commerce clause precludes a state from requiring persons selling extra-state eggs to post an announcement of that fact is discussed in 19 MICH. L. REV. 739.

F. Ry. Co. v. *Public Service Commission*[21] held invalid as an unreasonable interference with interstate commerce the order of a state commission requiring interstate trains to make a detour of ten miles to stop at a city of 4,000 inhabitants. The road as originally constructed ran through the town in question, but a later cut-off left the town on a side line. It still enjoyed seven local trains each way, some of which made connection with all through interstate trains. This was thought sufficient for local needs in view of the inconvenience to through traffic that would be caused by the desired routing of interstate trains.

In *Western Union Telegraph Co.* v. *Speight*[22] it was assumed that state law could not control the liability for delay in delivering interstate messages, and the question was whether a message sent between two points in a state over a route partly in another state was an interstate message. The court held that this must be tested by the actual transaction and that the message was interstate in fact. A question was raised whether the mode of transmission adopted was reasonable, but Mr. Justice Holmes answered that even if it were unreasonable as against the plaintiff any liability of the company, "if it existed, would not be a liability for an intrastate message that never took place but for the unwarranted conduct and the resulting loss." Mr. Justice Pitney confined his concurrence to the result.

In the course of holding that the state court had erred in respect to the doctrine of assumption of risk in rights of action under the federal Employers' Liability Law, Mr. Justice McKenna remarked in *Pryor* v. *Williams*[23] that the requirement of the federal act prevails over any state law. There appears to have been no dispute that the action was properly brought under the federal act. In two cases proceedings under state compensation acts were annulled because the employee was held to have been engaged in interstate commerce at the time of his injury and therefore to be confined to his action under the federal statute. *Philadelphia & Reading*

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[21] 254 U. S. 535, 41 Sup. Ct. 192 (1921).

[22] 254 U. S. 17, 41 Sup. Ct. 11 (1920). See 21 COLUM. L. REV. 270, 15 ILL. L. REV. 395, and 7 VA. L. REV. 225. A similar state case is considered in 19 MICH. L. REV. 227.

[23] 254 U. S. 43, 41 Sup. Ct. 36 (1920).

Ry. Co. v. *Di Donato*[24] involved a flagman employed by a railroad engaged in both interstate and intrastate commerce. He was held to be engaged in interstate commerce, even though flagging an intrastate train, since his duties were essential to the safety of all trains. Mr. Justice Clarke dissented. *Philadelphia & Reading Ry. Co.* v. *Polk*[25] had to do with an employee on a freight train carrying interstate and intrastate cars. The state court had approved of the award of compensation under the state act on the theory that the burden was on the defendant to show that the plaintiff was engaged in interstate commerce at the time of his injury and that there had been no such showing. Mr. Justice McKenna declared that the general duties of the employee caused him to be engaged in interstate as well as intrastate commerce and that the state court was unwarranted in presuming, in the absence of proof, that his duties were in intrastate commerce. He added that "the presumption, indeed, might be the other way," and observed that "it is to be remembered that it is the declaration of the cases that if there is an element of interstate commerce in a traffic or employment it determines the remedy of the employee." Mr. Justice Clarke again dissented, as he is apt to do when a decision is to the effect that the proceeding has been started under the wrong statute.[26]

One of the objections to a requirement to remove grade crossings which was before the court in *Erie Railroad Co.* v. *Board of Public Utility Commissioners*[27] was that the expense of compliance would interfere unwarrantably with interstate commerce, but Mr. Justice Holmes replied that "to engage in interstate commerce the railroad must get on to the land, and to get on to it must comply with the conditions imposed by the state for the safety of its citizens." Chief Justice White and Justices Van Devanter and McReynolds dissented, but whether on the commerce question or on the other grounds in the case does not appear.

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[24] 256 U. S. —, 41 Sup. Ct. 516 (1921)

[25] 256 U. S. —, 41 Sup. Ct. 518 (1921).

[26] For notes on cases on the question whether an action should be brought under state law or under the federal Employers' Liability Law, see 9 CALIF. L. REV. 260, 19 MICH. L. REV. 211, and 69 U. PA. L. REV. 290, 392.

The effect on state compensation laws of the federal Safety Appliance Act is discussed in 21 COLUM. L. REV. 389 and 30 YALE L. J. 732.

[27] 254 U. S. 394, 41 Sup. Ct. 169 (1921).

3. *State Taxation and Interstate Commerce*

In this review of constitutional decisions for 1919-1920[28] it was said that the question whether income from interstate commerce may be included in the assessment of a net income tax when the tax is a special one on corporations only and not a state-wide income tax was before the Supreme Court in cases contesting the corporation income tax law of Connecticut. The question was decided in the affirmative in *Underwood Typewriter Co.* v. *Chamberlain*[29] without adverting to the possibility of any distinction between taxes on all income from business within the state and taxes on corporate income only. The question whether such a tax may be imposed on a foreign corporation engaged exclusively in interstate commerce was not before the court, since the foreign corporation in question did some local business in Connecticut. Yet the opinion of Mr. Justice Brandeis suggests the inference that the exemption enjoyed by foreign corporations engaged exclusively in interstate commerce with respect to state excises on doing business within the state, when measured by some proportion of capital stock or imposed as a specific charge, will not be extended to excises measured by net income. After pointing out that payment of the tax is not a precedent to engaging in interstate commerce and that "the statute is, therefore, not open to the objection that it compels the company to pay for the privilege of interstate commerce," Mr. Justice Brandeis goes on to say:

> "A tax is not obnoxious to the commerce clause merely because imposed upon property used in interstate commerce, even if it takes the form of a tax for the privilege of exercising its franchise within the state. *Postal Telegraph Cable Co.* v. *Adams,* 155 U. S. 688, 695. This tax is based upon the net profits earned within the state. That a tax measured by net profits is valid, although these profits may have been derived in part, or indeed mainly, from interstate commerce, is settled. *U. S. Glue Co.* v. *Oak Creek,* 247 U. S. 321; *Shaffer* v. *Carter*, 252 U. S. 37, 57. Compare *Peck & Co.* v. *Lowe*, 247 U. S. 321. Whether it be deemed a property tax

[28] 19 MICH. L. REV. 34.
[29] 254 U. S. 113, 41 Sup. Ct. 45 (1920).

> or a franchise tax, it is not obnoxious to the commerce clause."

Further indication that a tax measured by net income will be judged by its effect, without regard to what kind of a tax "it be deemed," appears in the discussion whether the tax violates the Fourteenth Amendment because imposed on income from business outside the state, where Mr. Justice Brandeis says that "in considering this objection we may lay to one side the question whether this is an excise tax, purporting to be measured by the income accruing from business within the state, or a direct tax upon that income; for 'this argument, upon analysis, resolves itself into a mere question of definitions, and has no legitimate bearing upon any question raised under the federal Constitution.'" The phrase "any question" must include questions under the commerce clause as well as those under the Fourteenth Amendment. With technical distinctions as to the nature of the tax set to one side, net profits exclusively from interstate commerce should be subject to the same levy as net profits "mainly" from interstate commerce.

Taxation of the "intangible property" of a domestic corporation engaged exclusively in interstate commerce was sustained in *St. Louis & E. St. L. Electric Ry. Co.* v. *Missouri*[30] against the objection that it was a regulation of interstate commerce. The complainant was an electric railroad operating wholly on an interstate bridge. By the application of the unit rule its tangible property in Missouri was assessed for about $13,000 and "all other property" in Missouri for $173,000. This "other property" was obviously a capitalization of earning capacity. The company alleged that this "other property" consisted "solely of its franchise to conduct interstate passenger traffic over the interstate bridge," but Mr. Justice Clarke answered that the "large value" which the company concededly had "was derived, not from its mere franchise to do an interstate business, but from the exclusive right which we have seen the company acquired by private contract to operate over the Eads Bridge and from other rights also derived from private contract" to make its lines part of Illinois systems of suburban electric railroads. It was assumed that the assessment board must

[30] 256 U. S. —, 41 Sup. Ct. 488 (1921).

have taken these contracts into consideration and that therefore the claim that the tax was levied exclusively upon the franchise to do an interstate business was unsound. The applicable law developed in earlier decisions was stated as follows:

> "Slightly condensed, it is that, while a state may not, in the guise of taxation, constitutionally compel a corporation to pay for the privilege of engaging in interstate commerce, yet this immunity does not prevent the state from imposing an ordinary property tax upon property having a *situs* within its territory and employed in interstate commerce. Even the franchise of a corporation, if not derived from the United States, although that franchise is the business of interstate commerce, is subject to state taxation as part of its property."

This case was cited in *St. Louis-San Francisco Ry. Co.* v. *Middlekamp,*[31] decided the same day, for the proposition that a franchise tax on domestic corporations measured by the value of assets within the state is not invalidated because "the value of the franchise taxed is derived partly from the fact that the corporation does interstate business."

A license tax assessed at the specific sum of $60 on the local non-federal business of a telegraph company was sustained in *Postal Telegraph-Cable Co.* v. *Fremont*[32] as not a regulation of interstate commerce, although it was conceded that for the two years in question the company had conducted its intrastate business at a loss. Mr. Justice McKenna observed that the power to impose such license taxes on local business "of course has its limitations and must be exercised with due relation to the company's interstate business," but he pointed out that this relation "is not disposed of by the simple assertion of loss" and that "the cause of it or the condition of it is to be considered." He found the tax of $60 not "repellant from its amount" and noted that "there is no pretense that its imposition 'is a disguised attempt to tax interstate commerce.'" The fact that the company was compelled by the state to carry on intrastate business was held not controlling where the company had failed to avail itself of the privilege afforded by state law of petitioning

[31] 256 U. S. —, 41 Sup. Ct. 489 (1921).
[32] 255 U. S. 124, 41 Sup. Ct. 279 (1921).

the state railway commission for permission to increase its intrastate rates. With apparent approval, Mr. Justice McKenna noted that the state supreme court "expressed the view that mere proof of loss for two years, which may have been exceptional, determined nothing in the absence of a showing what business was available to the company or what facilities it had used." Though the court has several times recognized a principle that a specific license fee on unremunerative local business or a specific fee disproportionate to local business may be an invalid burden on interstate business, it has not thus far found a case to which the principle has been deemed applicable.[33]

That a license fee which falls indiscriminately and unescapably on the combined business of making domestic and interstate sales is wholly invalid is reaffirmed in *Bowman* v. *Continental Oil Co.*[34] This involved a fee of $50 for each place in which oil was distributed. The case arose in the federal district court, so that the state court had had no opportunity to declare that the demand was really imposed only on domestic sales. In refusing to reinterpret the statute so as to make it constitutional, Mr. Justice Pitney said:

> "No doubt the state might impose a license tax upon the distribution and sale of gasoline in domestic commerce if it did not make its payment a condition of carrying on interstate or foreign commerce. But the state has not done this by any act of legislation. Its executive and administrative officials have disavowed a purpose to exact payment of the license tax for the privilege of carrying on interstate commerce. But the difficulty is that, since plaintiff, so far as appears, necessarily conducts its interstate and domestic commerce in gasoline indiscriminately at the same stations and by the same agencies, the license tax cannot be enforced

[33] Cases on the question whether state inspection fees are so excessive as to be an invalid tax on interstate commerce are discussed in 34 HARV. L. REV. 333 and 19 MICH. L. REV. 209. Taxes on the interstate transmission of oil and gas are considered in 27 W. VA. L. Q. 345. For articles on state taxation and interstate commerce, see Thomas Reed Powell, "Taxation of Things in Transit," 7 VA. L. REV. 167, 245, 429, 497, and Cordenio A. Severance, "Gross Earnings Taxes Levied by States," 7 A. B. A. JOUR. 113.

[34] 256 U. S. —, 41 Sup. Ct. 606 (1921).

> at all without interfering with interstate commerce unless it be enforced otherwise than as prescribed by the statute—that is to say, without authority of law. Hence it cannot be enforced at all."

The method of enforcement referred to was a prohibition against the conduct of any business without payment of the fee. The same result would doubtless have been reached had the state provided for collection of the license fee by suit, for the imposition would still have been on all business, including interstate. This case was the second advent before the Supreme Court of the litigation considered the year before.[35] In addition to this license fee it involved an excise of two cents per gallon on all oil sold or used within the state. This tax was held divisible and invalid only as to oil sold in the original package in which it came from other states. Mr. Justice Pitney makes clear that the expression "in quantities to suit purchasers," used by Mr. Justice Day at the prior hearing, refers to sales which require the breaking of the original packages. So we know that if a company brings a barrel of oil into a state and sells half of it to one customer and half to another it is taxable on every gallon sold, while a sale of the whole barrel to a single customer is exempt, unless such sale is by a peddler or an auctioneer. The oil may be subjected to the general property tax, though still in the original package in the hands of the one who brought it into the state. The principal case holds also that "any and all oil used by the plaintiff" may be subjected to the excise of two cents per gallon. These nice distinctions between property taxes and sales taxes, between sales by peddlers or auctioneers and sales generally, between sales of parts of barrels and sales of whole barrels, and between sale and consumption have now been established by explicit adjudication, but they still await those substantial practical justifications which the law as the embodiment of perfect reason must be eager for the Supreme Court to give.

Another license tax on sales came before the court in *Bethlehem Motors Corporation* v. *Flynt*.[36] Here a Pennsylvania corporation

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[35] Askren v. Continental Oil Co., 252 U. S. 444, 40 Sup. Ct. 355 (1920), 19 MICH. L. REV. 32.

[36] 256 U. S. —, 41 Sup. Ct. 571 (1921).

shipped automobiles to North Carolina consignees who sold them from their storage warehouse. We are not told whether the sales were in the original packages or not. Persons selling cars within the state were subject to a $500 license fee unless the manufacturer had paid a similar tax to the state. This fee was reduced to $100 if the cars came from a manufacturer who invested three-fourths of his assets in property within the state or in the bonds of the state or of its municipalities. This obviously made it cheaper to sell cars manufactured within the state than cars made outside, since most local factories would be owned by companies having three-fourths of their assets within the state, and few if any extra-state factories would be in a similar situation. This discrimination was held invalid under the equal-protection clause if the complainant was a person within the jurisdiction, and invalid under the commerce clause if the complainant was still without the jurisdiction. Obviously, the discrimination should make the tax bad under the commerce clause, whether the sales were after the original package had been broken or not, and whether the complainants were technically persons within the jurisdiction or not. Mr. Justice McKenna's opinion on the commerce question is such a medley of different ideas that the only safe way to condense it is to give it in full:

> "If they [the complainants] are not within the state, their second contention is that the act is an attempt to regulate interstate commerce. If it have that effect it is illegal, for a tax on an agent of a foreign corporation for the sale of a product is a tax on the product, and if the product be that of another state it is a tax on commerce between the states. *Welton* v. *Missouri*, 91 U. S. 275; *Webber* v. *Virginia*, 103 U. S. 344; *Darnell & Son* v. *Memphis*, 208 U. S. 113. This is the assertion of plaintiffs in error; defendants in error interpose a denial to the assertion and the denial is supported by the Supreme Court [of North Carolina] on the authority of *Brown* v. *Houston*, 114 U. S. 622; *Sewing Machine Co.* v. *Bricknell*, 233 U. S. 304. The basis of the denial and its support by the Supreme Court is that the automobiles had passed out of interstate commerce and had reached repose in the state, and blend [*sic*] with the other things of the

> state, and because [*sic*] subject to interstate regulation. It is doubtful if that be a justifiable deduction from the findings of the trial court. But comment is not necessary. It is the finding of the court that the automobiles were in the hands of the agents of the consigning corporation and therefore, a tax against them was practically a tax on their importation into the state. It is not necessary to say it would be useless to send them to the state if their sale could be prevented by a prohibitive tax or one so discriminating that it would prevent competition with the products of the state. This is the ruling of the cases we have cited. It is especially the ruling in *Darnell & Son* v. *Memphis, supra.* This imposition of such a tax is practically the usurpation of the power of Congress over interstate commerce, and therefore illegal."

Some of this language, it is to be noted, goes beyond discriminatory taxes and beyond taxes on sales of articles in the original packages in which they entered the state. Justices Pitney and Brandeis dissent, but without opinion.

III. Taxation

1. *Federal Taxes*

The federal income, excess profits, and estate taxes brought to the Supreme Court some fundamental constitutional questions which it found easy to answer in favor of the government. The contention that profit from the sale of corporate stock or other property when realized by a non-trader is capital and not income under the Sixteenth Amendment was dismissed by quotation of definitions from previous opinions and on the authority of decisions under the Corporate Excise Tax of 1909, which had been recognized *obiter* as settling that such profit is income under the Amendment. Troublesome statements in earlier opinions that such a profit is capital and not income were rejected as *obiter dicta* or as confined to the interpretation of particular statutes. The opinions of Mr. Justice Clarke in the four cases[37] declaring and apply-

[37] The cases are the ones cited in notes 38-41 *infra*. For notes on the Supreme Court decisions, see 34 Harv. L. Rev. 781, 16 Ill. L. Rev. 68, 19 Mich.

ing this definition of income contain no analysis of the objections thus summarily disposed of. The court was unanimous, but the reporter states that "Mr. Justice Holmes and Mr. Justice Brandeis, because of prior decisions of the court, concur only in the judgment."

In *Merchants' Loan & Trust Co.* v. *Smietanka*[38] the profit in question was realized by a trustee under a will which provided that "accretions of selling values should be considered principal and not income." The contention that this profit is not income to the life-tenant because she does not get it, and not income to the remaindermen because they do not get it and may never get it, was answered by saying that for the purpose of taxation it is to be treated as if the trustee were the sole owner. The fact that the profit was realized by a single sale by a non-trader was held of no importance. Cases holding that such profit realized by a trustee must be credited to the principal of the trust and not to income were said to be "of little value in determining such a question as we have here." British income tax decisions were also put aside as "without value" because of the particular British statutes of which they were interpretations. No mention was made of the point that the profit was treated as income for the year in which it was realized, although only a part of the gain accrued in that year.

In *Eldorado Coal & Mining Co.* v. *Mager*[39] the profit taxed as income was that realized by a corporation upon a disposition of its entire plant preparatory to winding up its business. The corporation was not formally dissolved during the tax year in question on account of unsettled liabilities for various federal taxes.

In *Goodrich* v. *Edwards*[40] and *Walsh* v. *Brewster*[41] individuals

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L. REV. 854, 5 MINN. L. REV. 568, and 68 U. PA. L. REV. 380. For discussions prior to the Supreme Court decisions, see Fred R. Fairchild and Robert M. Haig, "Is Increase in the Value of Capital Income?" 6 BULL. NAT. TAX ASSN. 213; Thomas Reed Powell, "Income from Sales of Investments," 6 BULL. NAT. TAX ASSN. 137; and notes in 21 COLUM. L. REV. 163, 34 HARV. L. REV. 564, 15 ILL. L. REV. 535, 5 MINN. L. REV. 238, 69 U. PA. L. REV. 253, 6 VA. L. REG. n. s. 847, 868, and 30 YALE L. J. 396, 428.

[38] 255 U. S. —, 41 Sup. Ct. 386 (1921).

[39] 255 U. S. —, 41 Sup. Ct. 390 (1921).

[40] 255 U. S. —, 41 Sup. Ct. 390 (1921).

[41] 255 U. S. —, 41 Sup. Ct. 392 (1921).

were held subject to the income tax on profit realized from the sale of corporate stock and bonds. The court held that the statute meant to tax no more than the actual gain on the transaction when the original purchase price was higher than the later value of the property on March 1, 1913, the effective date of the Sixteenth Amendment. It was clear enough that the statute meant to tax no more than the amount by which the sale price exceeded the value on March 1, 1913, but the tax authorities had insisted that this amount was taxable as income, even though the value on that date was less than the original cost, thus claiming that there may be taxable income even though the entire transaction yields a loss. During the argument the solicitor general conceded that this construction was erroneous and the court agreed with him, thus avoiding the necessity of deciding whether the interpretation previously insisted upon by the internal revenue department could satisfy the conception of income under the Sixteenth Amendment. The *Brewster* case held also that loss of interest on an investment could not be regarded as part of the original cost, even when this loss was a stipulated part of the purchase transaction prior to the effective date of the Sixteenth Amendment. Without analysis, the claim of the taxpayer was declared to be answered by a decision in a case under the Corporation Excise Tax of 1909.[42]

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[42] United States v. Woodward, 256 U. S. —, 41 Sup. Ct. 615 (1921), held that under the Act of 1918 the amount paid to the United States as an estates tax may be deducted from gross income in reaching the amount to be assessed for the income tax. The decision to the same effect in the Court of Claims is commented on in 30 YALE L. J. 770.

A decision of the Circuit Court of Appeals for the Second Circuit, which the Supreme Court declined to review on request for certiorari, held that under the federal income tax law of 1913 an individual cannot deduct from his income the amount paid for an inheritance tax under the statute of New York. This point is considered in 19 MICH. L. REV. 348 and 30 YALE L. J. 199.

Other questions of the interpretation of federal income tax laws are dealt with in 34 HARV. L. REV. 220, 15 ILL. L. REV. 339, 342, 534, 19 MICH. L. REV. 103, and 7 VA. L. REV. 131, 151. Disputes as to deductions under the Corporation Excise of 1909 are treated in 30 YALE L. J. 636, 636 (two notes).

Evans v. Gore, 253 U. S. 245, 40 Sup. Ct. 550 (1920), 19 MICH. L. REV. 117, which held that a tax on the salary of a federal judge is a diminution thereof within the constitutional prohibition against diminution, is consid-

The constitutionality of the excess profits tax was affirmed in *La Belle Iron Works* v. *United States*.[43] Here again the court was unanimous, though Mr. Justice McReynolds confined his concurrence to the result. The statute in question imposes a graduated tax on the net income from certain trades and businesses in excess of the deduction allowed. The deductions are reached by taking certain percentages of the invested capital of the business. Income in excess of these percentages is subjected to a progressive tax in addition to the general income tax on corporations and individuals. Thus, the higher the invested capital the greater the deduction and the less the tax. The claimant before the court had, prior to 1904, acquired certain assets at a cost of $190,000, which by 1912 had become worth not less than $10,105,400. This increase was due in part to explorations and developments, but the cost of these activities was not disclosed by the claimant, so that the appreciation was treated as an "unearned increment." In interpreting the statute the court confined the "invested capital" to the capital invested, and excluded appreciation since the original acquisition of the property.

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ered in 20 COLUM. L. REV. 794, 34 HARV. L. REV. 70, 85, 5 MINN. L. REV. 145, 7 VA. L. REV. 69, 76, and 30 YALE L. J. 76.

Eisner v. Macomber, 252 U. S. 189, 40 Sup. Ct. 189 (1920), 19 MICH. L. REV. 118, which held stock dividends not income under the Sixteenth Amendment, is discussed in Eustace Seligman, "Implications and Effects of the Stock Dividend Decision," 21 COLUM. L. REV. 313; and a note in 7 VA. L. REV. 134.

For other discussion of federal income taxation, see Arthur A. Ballantine, "Corporate Personality in Income Taxation," 34 HARV. L. REV. 573; Raymond G. Brown, "The Sixteenth Amendment to the United States Constitution," 54 AM. L. REV. 843; Harry Hubbard, "From Whatever Source Derived," 6 A. B. A. JOUR. 203; A. E. James, "Tax Exemptions in the Income Tax," 6 BULL. NAT. TAX ASSN. 238; George E. Putnam, "Income Tax Exemption," 6 BULL. NAT. TAX ASSN. 75; William S. Rea, "Exemption of State and Municipal Bonds from Federal Income Tax," 25 LAW NOTES 5; and Hugh Satterlee, "Simplification of Federal Taxation," 6 BULL. NAT. TAX ASSN. 72.

[43] 256 U. S. —, 41 Sup. Ct. 528 (1921). For discussions of the issue prior to the Supreme Court decisions, see Arthur A. Ballantine, "Some Constitutional Aspects of the Excess Profits Tax," 29 YALE L. J. 625, and Charles McCamic, "Appreciation in Value as Invested Capital Under the Excess Profits Law," 30 YALE L. J. 239.

This taking of original cost instead of present value was alleged by the taxpayer to have "the effect of rendering the act 'glaringly unequal and of doubtful constitutionality; the insistence being that, so construed, it operates to produce baseless and arbitrary discriminations, to the extent of rendering the tax invalid under the due-process clause of the Fifth Amendment." In meeting this objection Mr. Justice Pitney made no mention of the position taken by Chief Justice White in earlier cases that the Fifth Amendment does not limit the federal taxing power. He put aside certain decisions under the equal-protection clause of the Fourteenth Amendment as clearly not in point, because "the Fifth Amendment has no equal protection clause," and reiterated the established ruling that the only requirement of uniformity in federal indirect taxes is of geographical uniformity against which the excess profits tax concededly commits no offense. He prefaced his consideration of the alleged unreasonable discriminations by saying:

> "Nor can we regard the act—in basing 'invested capital' upon actual costs to the exclusion of higher estimated values —as productive of arbitrary discriminations raising a doubt about its unconstitutionality under the due-process clause of the Fifth Amendment. The difficulty of adjusting any system of taxation so as to render it precisely equal in its bearing is proverbial, and such nicety is not even required of the states under the equal-protection clause, much less of Congress under the more general requirement of due process of law in taxation. Of course it will be understood that Congress has very ample authority to adjust its income taxes according to its discretion, within the bounds of geographical uniformity. Courts have no authority to pass upon the propriety of its measures; and we deal with the present criticism only for the purpose of refuting the contention, strongly urged, that the tax is so wholly arbitrary as to amount to confiscation."

This seems to make confiscation rather than arbitrary discrimination the only possible offense under the Fifth Amendment, thus attaching importance to discrimination only as the more favorable

position of competitors may result in confiscation of the property or business of the less privileged. Mr. Justice Pitney, however, does not make this explicit nor does he give any elucidation of what the court means by "confiscation." He goes on to say that "the act treats all corporations and partnerships alike, so far as they are similarly circumstanced," and that if the valuation of capital "according to what actually was embarked at the outset or added thereafter, disregarding any appreciation in values," makes the tax in particular instances "seem to bear upon one corporation more than upon another, this is due to difference in their circumstances, not to any uncertainty or want of generality in the tests applied." The reasonableness of taking cost as a basis is predicated on its superior certainty and on the "logical incongruity" of taking estimates of values which could be realized only by a sale that would require the abandonment of the purpose for which the property is held. Reference is made to the customary practice of issuing different classes of securities, bonds, preferred stock and common stock, for different kinds of contribution to corporate capital, and it is concluded that "upon like grounds it was not unreasonable for Congress, in adjusting the 'excess profits tax,' to accord preferential treatment to capital representing actual investments, as compared with capital representing higher valuations based upon estimates, however confident and reliable, of what probably could be realized were the property sold instead of retained."

The federal estates tax was unanimously sustained in *New York Trust Co.* v. *Eisner*[44] against the objections that it is unequal, that it is a direct tax not apportioned as the Constitution requires, and that it is an unconstitutional interference with the right of the states to regulate descent and distribution. The third objection will be dealt with in a later section on intergovernmental relations. The contention that the tax is direct was based upon the fact that, being on the estate, it is inevitable, and not, like a legacy tax on the privilege of receiving, avoidable and so indirect. "That matter," answered Mr. Justice Holmes, was disposed of by the case sustaining a federal legacy tax, "not by an attempt to make some

[44] 256 U. S. —, 41 Sup. Ct. 506 (1921).

scientific distinction, which would be at least difficult, but on an interpretation of language by its traditional use—on the practical and historical ground that this kind of a tax always has been regarded as the antithesis of a direct tax; 'has ever been treated as a duty or excise, because of the particular occasion which gives rise to its levy.'" "Upon this point," he adds, "a page of history is worth a volume of logic." He disposes of the complaint of inequality by saying:

> "The inequalities charged upon the statute, if there is an intestacy, are all inequalities in the amounts that beneficiaries might receive in cases of estates of different values, of different proportions between real and personal estate, and of different numbers of recipients; or if there is a will affecting legatees. As to the inequalities in case of a will, they must be taken to be contemplated by the testator. He knows the law and the consequences of the dispositions that he makes. As to intestate successors, the tax is not imposed upon them but precedes them, and the fact that they may receive less or different sums because of the statute does not concern the United States."

The objections thus dismissed were doubtless based upon the fact that the federal tax reduces the estate as a whole instead of taking from each beneficiary according to the amount coming to him from the deceased. In construing the act the court allowed no deduction of state inheritance and succession taxes. The reason appeared to be that all the state taxes in question were "taxes on the right of individual beneficiaries" and "not charges that affect the estate as a whole," and hence not "charges against the estate" in the words of the federal act. It is not intimated that this construction was objected to on constitutional grounds. The reasoning leaves open the possibility of a different attitude toward the deduction of state taxes on the estate as a whole. What amount the state may take as a basis of taxation, and questions of priority between the United States and the state were said not to be open in the particular case.[45]

[45] Certain aspects of the application of the federal estates tax to the American assets of foreigners are treated in Julius Goebel, Jr., "The Return on Estates of Non-resident Decedents," 7 VA. L. REV. 343.

In *United States* v. *Field*[46] the Act of 1916 was interpreted not to include in the estates tax property passing under a testamentary execution of a general power of appointment created prior to the enactment of the statute. That a later statute specifically including such an execution will be sustained as constitutional is likely from Mr. Justice Pitney's citations in the principal case following his statement that no question is "suggested as to the power of Congress to impose a tax upon the passing of property under testamentary execution of a power of appointment created before, but executed after, the passage of the taxing act."[47]

A concededly drastic method of preventing or penalizing the evasion of federal tax laws was sustained in *Goldsmith-Grant Co.* v. *United States*.[48] An Act of 1866 provided for the forfeiture of any conveyance used in transporting commodities removed with intent to evade a tax thereon. Under this provision the government seized an automobile in which untaxed liquor was transported. Title to the car was in a conditional vendor who was entirely innocent of any complicity in its unlawful excursion. He contended that the statute ought not to be construed to command a forfeiture of his interest, and that if so construed it denied due process of law. The court reserved opinion as to whether the statute could be extended to property stolen from the owner or otherwise taken from him without his privity or consent, and put to one side as a danger not yet realized the possibility that it might forfeit a Pullman car or an ocean steamship. Mr. Justice McKenna conceded that there is strength to the contention that the forfeiture of the interest of any innocent owner "seems to violate that justice which should be the foundation of the due process of law required by the Constitution," but against it he found "other and militating considerations." The important one seemed to be the necessity of adequate provision against evasion of the revenue laws. With respect to certain kinds of property that are facilities for such eva-

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[46] 255 U. S. 257, 41 Sup. Ct. 256 (1921).

[47] Another problem in interpreting the federal estates tax law is dealt with in 5 MINN. L. REV. 78.

[48] 254 U. S. 505, 41 Sup. Ct. 189 (1921). See 15 ILL. L. REV. 613 and 69 U. PA. L. REV. 189. A somewhat similar issue is treated in 5 MINN. L. REV. 482.

sion "Congress interposes the care and responsiblity of their owners in aid of the prohibitions of the law and its punitive provisions, by ascribing to the property a certain personality, a power of complicity and guilt in the wrong." The analogy of the deodand is referred to and Blackstone is quoted for the practical justification "that such misfortunes are in part owing to the negligence of their owner, and therefore he is properly punishable by such forfeiture." Sir William's references to Moses and to the Athenians are also quoted, and it is concluded that whether the reason for the forfeiture "be artificial or real, it is too firmly fixed in the punitive and remedial jurisprudence of the country to be now displaced." Old ways did not make so strong an appeal to Mr. Justice McReynolds and he therefore dissented.[49]

In *Minnesota* v. *Martinson*[50] a defendant who had violated a state police regulation of the sale of habit-forming drugs contended that the state law was void for interference with the collection of the federal tax on dispensers of such drugs, but the court was unable to find the interference alleged.

The chief complaint urged against the Connecticut excise on

[49] In holding that under the applicable federal statutes failure to appeal to the commissioner of internal revenue after payment of a tax precluded suit for a refund against the government, even though an application for abatement was made to the commissioner before payment, Mr. Justice Holmes remarked in Rock Island, A. & L. R. Co. v. United States, 254 U. S. 141, 41 Sup. Ct. 55 (1920):

> "Men must turn square corners when they deal with the Government. If it attaches even purely formal conditions to its consent to be sued, those conditions must be complied with. *Lex non praecipit inutilia* (Co. Lit. 127b) expresses rather an ideal than an accomplished fact. But in this case we cannot pronounce the second appeal a mere form. On appeal a judge sometimes concurs in a reversal of his decision below. It is possible, as suggested by the Court of Claims, that the second appeal may be heard by a different person. At all events, the words are there in the statute and the regulations, and the Court is of opinion that they mark the condition of the claimant's right."

An effort to secure repayment of a legacy tax under the Act of 1898 failed in Cochran v. United States, 254 U. S. 387, 41 Sup. Ct. 166 (1921); one to get back an excise tax on chewing gum, in United States v. American Chicle Co., 256 U. S. —, 41 Sup. Ct. 548 (1921).

[50] 256 U. S. —, 41 Sup. Ct. 425 (1921).

corporations in *Underwood Typewriter Co.* v. *Chamberlain*[51] was that the state had adopted an improper ratio for determining how much of the total income of a Delaware corporation was derived from Connecticut sources. Connecticut allocated to itself so much of the total income of manufacturing corporations as their tangible property in Connecticut bears to their tangible property everywhere. Under this rule 47 per cent of the total income of the Underwood Company was taken as the measure of the Connecticut tax, although of its total net receipts $1,293,643.95 was received in other states and only $42,942.18 in Connecticut. Of this situation Mr. Justice Brandeis said:

> "But this showing wholly fails to sustain the objection. The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut and ending with sale in other states. In this it was typical of a large part of the manufacturing business conducted within the state. The legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It therefore adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state. 'The plaintiff's argument on this branch of the case,' as stated by the Supreme Court of Errors, 'carries the burden of showing that 47 per cent of its net income is not reasonably attributable, for purposes of taxation, to the manufacture of products from the sale of which 80 per cent of its gross earnings were derived after paying manufacturing costs.' The corporation has not even attempted to show this; and for aught that appears the percentage of net profits earned in Connecticut may have been much larger than 47 per cent. There is, consequently, nothing in this record to show that the method of apportionment adopted by the state was inherently arbi-

[51] 254 U. S. 113, 41 Sup. Ct. 45 (1920). See Harold S. Lyon, "Allocation of Net Income from Interstate Business," 6 BULL. NAT. TAX ASSN. 172; and comments in 30 YALE L. J. 512, 534. The decision of the court below is discussed in 20 COLUM. L. REV. 324 and 33 HARV. L. REV. 736.

> trary, or that its application to this corporation produced an unreasonable result."

This is to say merely that the complainant has not proven its case. Mr. Justice Brandeis adds that there is "no occasion to consider whether the rule prescribed, if applied under different conditions, might be obnoxious to the Constitution." It is worthy of note that the Underwood people's objection that the tax was in reality in considerable measure on extra-state income is referred by the Supreme Court to the Fourteenth Amendment alone and not to a combination of the Fourteenth Amendment and the commerce clause, as in most if not all of the prior cases dealing with corporate excises measured by property outside the taxing state. Previous opinions have left it doubtful whether a due-process objection alone would be sufficient to annul excises on foreign corporations measured in ways that include extra-territorial values. In the *Underwood* case there is no indication that any help from the commerce clause is needed to invalidate corporate excises found to be in substance taxes on property or income without the state. Moreover, in the opinion sustaining the federal excess profits tax.[52] Mr. Justice Pitney refers to due process alone the cases which have found corporate excises guilty of the vice of extra-territoriality when he says:

> "Appellant cites *Looney* v. *Crane Co.*, 245 U. S. 178, 188, and *International Paper Co.* v. *Massachusetts*, 246 U. S. 135, 145, but these cases also are inapplicable, being based upon the due process clause of the Fourteenth Amendment, with which state taxing laws were held in conflict because they had the effect of imposing taxes on the property of foreign corporations located and used beyond the jurisdiction of the taxing state."

This makes it certain that *Horn Silver Mining Co.* v. *New York*,[53] though not yet explicitly overruled, is no longer law.[54]

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[52] La Belle Iron Works v. United States, note 43, *supra*.

[53] 143 U. S. 305, 12 Sup. Ct. 403 (1892).

[54] Questions of jurisdiction or of matters somewhat related thereto are considered in Walter Clark, "Can Shares of Stock be Exempted from Taxation in the Hands of Shareholders?" 54 AM. L. REV 689; Edward L. Leahy,

A transfer tax on transfers in contemplation of death was sustained in *Nickel* v. *Cole*[55] against the complaint that it violated the Fourteenth Amendment because of retroactivity. A Nevada statute was passed on March 26, 1913, to go into effect thirty days later. Before the thirty days were up a California resident transferred to trustees stock in a Nevada corporation which owned a California corporation which owned Nevada land. It was conceded that the transfer would be constitutionally taxable if the statute had been in operation at the time it was made, but it was insisted that the interest of the remaindermen after the death of the life tenant and creator of the trust had vested upon the execution of the deed prior to the effective date of the statute. The Supreme Court answered that a statute passed before the date of the deed might have been so drawn as to tax the deed and that a construction by the state court that it did in fact do so would have been good as against any objection under the federal Constitution. Even if the state court in reaching this construction went on the untenable ground that the deed and a contemporaneous will formed parts of a single transaction under which no vested right arose until the death of the grantor and testator, this was wholly a question of state law which

"Rule of Apportionment of Corporate Property Upheld," 6 BULL. NAT. TAX ASSN. 39; Thomas Reed Powell, "Taxation of Things in Transit," 7 VA. L. REV. 167, 245, 429, 497; notes in 21 COLUM. L. REV. 362 and 30 YALE L. J. 529 on when a foreign corporation is doing business within the state; in 34 HARV. L. REV. 95 on a tax at the domicile on a resident's seat in a foreign stock exchange; and in 34 HARV. L. REV. 542, 564, on a personal tax on a non-resident temporarily present within the taxing jurisdiction.

For consideration of problems of state income taxation, see Robert Whitehead, "The Income Tax Laws of Virginia," 6 VA. L. REG. n. s. 721; and notes in 21 COLUM. L. REV. 294 and 1 WIS. L. REV. 192 on whether certain receipts of insurance companies are income.

The Illinois capital stock tax is discussed in 15 ILL. L. REV. 455; the question whether power has been delegated to a municipality to impose a license tax on attorneys, in 5 MINN. L. REV. 548; other questions of state taxation, in Thomas K. Skinker, "Constitutional Limitations on Municipal Taxation in Missouri," 6 ST. LOUIS L. REV. 61; and E. J. Verlie, "Property Tax Exemption in Illinois," 3 ILL. L. B. 142.

In Dawson v. Kentucky Distilleries Co., 255 U. S. 288, 41 Sup. Ct. 272 (1921) what purported to be an excise tax on removing liquor from bond was declared to be in effect a property tax and void as such under the Kentucky Constitution. The point is treated in a note in 35 HARV. L. REV. 70.

[55] 256 U. S. —, 41 Sup. Ct. 467 (1921).

the Supreme Court will accept, whether right or wrong, since there can be no pretense that the state court adopted its view to evade an issue under the federal Constitution. "When, as here," concluded Mr. Justice Holmes, "the statute unquestionably might have made the tax applicable to this transfer, we do not inquire very curiously into the reasoning by which the statute is held to justify the tax."[56]

Complaints that the procedure for assessing taxes did not include the hearing requisite to due process were dealt with in two cases. In *Turner* v. *Wade*[57] the procedure was held inadequate. The only hearing offered the taxpayer was one before arbitrators after the assessors had notified him of an increase of the valuation returned by him. Unless a majority of the arbitrators agreed upon a decision within ten days after being named, the valuation of the assessors was to stand. In the case at bar the three arbitrators all agreed that the assessors had placed too high a valuation on the property, but each arbitrator insisted on a different valuation, and so, for want of a majority agreement, the valuation of the assessors stood. In the principal case, therefore, such hearing as the taxpayer had was not before the body that fixed the assessment. The case was disposed of on the understanding that the state conceded "that the provision for arbitration, under the facts herein shown, does not of itself afford due process of law" and that the issue was whether the law provided for an adequate hearing before the board of assessors. The Supreme Court found that the state court had construed the statute so as to provide for no hearing before this board, and concluded that "in the present case, as the facts stated show, the taxpayer is subject to an assessment made without notice and hearing," and so is denied due process of law.

An opposite result was reached in *St. Louis-San Francisco Ry. Co.* v. *Middlekamp*,[58] in which the tax might be collected only by suit in which it was assumed that all questions of law apparent on

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[56] Inheritance tax problems are considered in Joseph H. Matthews, "Proposed Flat Rate upon the Transfer at Death of Personal Property of Nonresidents," 6 BULL. NAT. TAX ASSN. 132; and a note in 34 HARV. L. REV. 441 on whether the federal inheritance tax may be deducted before assessing the state inheritance tax.

[57] 254 U. S. 64, 41 Sup. Ct. 27 (1920). See 21 COLUM. L. REV. 284.

[58] 256 U. S. —, 41 Sup. Ct. 489 (1921).

the face of the record would be open and that the only questions which the particular contestant would raise could be urged by it. The decision appears to be based on the conclusion that the statute allowed the court to consider any matter in which the particular complainant in this particular instance was interested and to invite the inference that this is sufficient even though the statute might withhold the requisite hearing in other controversies than the one under adjudication. All that Mr. Justice Holmes has to say on this branch of the case is as follows:

> "The objection most insisted upon in this court was that the statute made no provision for a hearing, and that although the plaintiff applied to the Tax Commission for a hearing and had one, the statute was bad because it did not provide one in terms. *Central of Georgia Ry. Co.* v. *Wright,* 207 U. S. 127, 138. The mode of collecting the tax is by a suit where, of course, the present plaintiff would be heard, but it is said that the judgment of the Commission can be attacked only for want of jurisdiction and fraud. We cannot suppose, however, that any question of law apparent on the face of the record would not be open. The constitutional objection mainly relied upon necessarily would be. And as in this case the commission acepted the plaintiff's figures, and the contest is wholly upon matters of law, we see nothing of which the plaintiff can complain in this respect. There is, to be sure, one charge involving matters of fact *dehors* the record. It is alleged that the plaintiff was taxed disproportionately as compared with other railroads. But the plaintiff was taxed upon its own figures in accordance with the statute and could not complain of that. If it had made out a case of fraud against the Commission we presume that the state courts would have been open to it, as well as the District Court of the United States. But nothing of that kind was proved. *Sunday Lake Iron Co.* v. *Wakefield,* 247 U. S. 350, 353."

The *Middlekamp* case hinted also at a contention that the domestic corporation before the court was denied the equal protection of the laws because its tax was based on its Missouri assets, while certain foreign corporations with stock having no stated par value

were admitted to the state and subjected only to a tax of $25 imposed upon foreign corporations without capital stock; but the contention was not considered because the court was not convinced that these corporations with no-par stock in fact enjoyed the supposed more favorable treatment. So also, in *Underwood Typewriter Co.* v. *Chamberlain,*[59] some unspecified contention based on the Fourteenth Amendment and the fact that the foreign corporation objecting to the corporation income tax had made large permanent investments in the state before the law was enacted was said to be clearly unsound. That the objection was to some supposed discrimination is to be inferred from the statement in the opinion that "to the facts presented here the principle discussed in *Southern Railway Co.* v. *Greene,* 216 U. S. 400, 414, has no application."

In five cases complaints against discrimination were squarely raised, and in all but one the differences of treatment were held proper. *Watson* v. *New York*[60] sustained the provision in the New York inheritance tax imposing an additional five per cent on the transfer of investments on which the decedent had during the designated period preceding his death paid neither the general property tax nor the optional stamp tax. The complainant conceded that classification is reasonable if based on the kind or amount of value of the property transferred or on the relationship or the character of the transferees; but this list, said Mr. Justice Brandeis, "does not exhaust the possibilities of legal classification." It is enough that the classification "has a reasonable relation to some permitted end of governmental action." The justification for the particular classification is put in the rhetorical query: "And what classification could be more reasonable than to distinguish, in imposing an inheritance or transfer tax, between property which had during the decedent's life borne its fair share of the tax burden and that which had not?" The court found it unnecessary to consider whether the tax would have violated the Fourteenth Amendment as a property tax or as a penalty, for it held it not the former, although it might induce owners of investments to present them

[59] Note 51, *supra.*

[60] 254 U. S. 122, 41 Sup. Ct. 43 (1920). A state decision on the same question is treated in 20 Colum. L. Rev. 625.

for taxation, and not the latter, although it might take a heavier toll than would the taxation to which the owner might have subjected himself in his lifetime.

The discrimination involved in the Alaska license tax on persons manufacturing fish oil, fertilizer and fish meal in whole or in part from herring, which was sustained in *Alaska Fish Salting & By-Products Co.* v. *Smith*,[61] was produced by the immunity enjoyed by persons using other fish for the same purposes and by persons using herring for other purposes. Though the objection was necessarily founded on the Fifth rather than on the Fourteenth Amendment, and the former contains no equal-protection clause, the basis of the decision was that the discrimination was reasonable and the case, it is to be assumed, may be taken as a precedent for the interpretation of the equal-protection clause of the Fourteenth Amendment. In support of the result Mr. Justice Holmes said:

> "If Alaska deems it for its welfare to discourage the destruction of herring for manure and to preserve them for food for man or for salmon, and to that end imposes a greater tax upon that part of the plaintiff's industry than upon similar use of other fish or of the offal of salmon, it hardly can be said to be contravening a Constitution that has known protective tariffs for a hundred years. * * * Even if the tax should destroy a business it would not be made invalid or require compensation upon that ground alone. Those who enter upon a business take that risk. * * * We need not consider whether abuses of the power might go to such a point as to transcend it, for we have not such a case before us. The Acts must be judged by their contents, not by the allegations as to their purposes in the complaint. We know of no objection to exacting a discouraging rate as the alternative to giving up a business when the legislature has the full power of taxation. The case is different from those where the power to tax is limited to inspection fees and the like."

The excise on the sale and use of oil, which was sustained in

[61] 255 U. S. 44, 41 Sup. Ct. 219 (1921).

Bowman v. *Continental Oil Co.*[62] as applied to oil no longer in the original package in which it entered from other states, was unsuccessfully attacked as a denial of due process and of equal protection of the laws. Without stating the objection, Mr. Justice Pitney declared it to be without substance. The complaint was doubtless the same as that urged under the clause of the state constitution requiring that taxes shall be equal and uniform upon subjects of taxation of the same class. As to this Mr. Justice Pitney said:

> "We see no reason to doubt the power of the state to select this commodity, as distinguished from others, in order to impose an excise tax upon its sale and use; and since the tax operates impartially upon all, and with territorial uniformity throughout the state, we deem it 'equal and uniform upon subjects of taxation of the same class' within the meaning of Section 1 of Article 8."

The equal-protection clause was also unsuccessfully invoked in *Dane* v. *Jackson*[63] against the provisions of the Massachusetts income tax, under which certain towns received back from the state considerably less than the tax collected from their residents. Mr. Dane thought that he was discriminated against by making contributions to the support of towns remote from home while persons in other towns not only found the bread which they cast upon the waters returned to their own bailiwick but also benefited from some of the bread that he had cast. In reply Mr. Justice Clarke told him how hard it is to have an exactly equal or proportional system of taxation and assured him that Massachusetts had stopped short of that arbitrariness which is necessary to make a tax offend against the Fourteenth Amendment. The present scheme was devised in part to overcome the advantages which wealthy persons derived from "colonization" in towns with low tax rates, and this was thought to be a legitimate end of legislative endeavor. A due-process objection was held as futile as that based on the equal-protection clause.

In one case objection to discrimination was held to be well

62 256 U. S. —, 41 Sup. Ct. 606 (1921).

63 256 U. S. —, 41 Sup. Ct. 566 (1921).

founded. This was *Bethlehem Motors Corporation* v. *Flynt,*[64] already considered in the section on regulations of interstate commerce. Here was a fee of $500 for selling automobiles within the state which was reduced to $100 if the manufacturer invested three-fourths of his assets in the bonds of the state or of its counties or cities or in property within the state. The Supreme Court saw readily enough that all extra-state manufacturers or their agents would be liable for the $500 fee while most local manufacturers or their agents would pay only $100. This was held to be a denial of equal protection of the laws. The question was whether the complainants were "persons within the jurisdiction" so as to come within the scope of the equal-protection clause. The test laid down to determine when foreign corporations become persons within the jurisdiction is as follows:

> "(1) If the Pennsylvania corporation and the Indiana corporation and the Delaware corporation are doing business in the state, and therefore within its jurisdiction, they undoubtedly can complain of a discrimination against them that is offensive to the Fourteenth Amendment. *Southern Railway Co.* v. *Greene,* 216 U. S. 400. (2) If, however, they are not in the state and subject to its jurisdiction, and seek to enter, the tax may be considered a condition which the state may impose. *Paul* v. *Virginia,* 8 Wall. 168, and a number of subsequent cases, including *Southern Railway Co.* v. *Greene, supra.* * * *
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> "This court has decided too often to need citation of the cases that corporations doing business in a state and having an agent there are within the jurisdiction of the state for the purpose of suit against them, and we may assume that the principle is applicable here and that the Pennsylvania corporation, the Indiana corporation and the Delaware corporation are within the jurisdiction of the state and subject to its laws, equally with the corporations of the state."

This makes the test of being within the jurisdiction for service of process the test of being within the jurisdiction so as to claim the equal protection of the laws. It omits all mention of formal admis-

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[64] 256 U. S.—, 41 Sup. Ct. 571 (1921).

sion to do business and of the acquisition of a large amount of property of a permanent character—two elements present in the *Greene* case and emphasized as important in making the foreign corporation there involved a person within the jurisdiction. For all that appears in Mr. Justice McKenna's opinion in the principal case, a foreign corporation which actually does business through agents in a state in violation of valid state laws nevertheless becomes a person within the jurisdiction so as to be entitled to equal protection of the laws. The statement of facts shows that the consignees within the state were agents of the extra-state manufacturers for the purpose of selling and delivering their cars, but there is no evidence that the manufacturing corporation had been formally admitted to do business in the state or had complied with any state laws applying to foreign corporations. Under this state of facts Mr. Justice McKenna seems to lay down a rule which puts it in the power of any foreign corporation to become a person within the jurisdiction by merely sneaking in through agents, provided they do enough business to make the corporation subject to service of process. This ruling, however, was not necessary to the disposition of the case, since it held that if the corporation was not within the jurisdiction the tax is invalid under the commerce clause. Though the opinion says that "we may assume" that the foreign corporations were within the jurisdiction, there are other expressions which support an inference that the court did not mean to decide the specific point, but was content to hold the tax bad for violation either of the equal-protection clause or of the commerce clause, without specifying which. Justices Pitney and Brandeis dissented without stating their objections.[65]

Three cases had to do with special assessments. In two the complaints of the taxpayers were held to be unfounded. In *Miller & Lux, Inc.* v. *Sacramento & San Joaquin Drainage District*[66] a land owner assessed five cents per acre for general preliminary expenses for a drainage improvement found fault because the statute gave it

[65] In 20 COLUM. L. REV. 793 is a discussion of F. S. Royster Guano Co. v. Virginia, 253 U. S. 412, 40 Sup. Ct. 560 (1920), 19 MICH. L. REV. 126, which held it a denial of equal protection to tax some domestic corporations on extra-state income while that of others went free.

[66] 256 U. S. —, 41 Sup. Ct. 404 (1921).

no opportunity to show that its lands would receive no special or direct benefit from the proposed improvement, but the court deemed the complaint so unsubstantial as to require dismissal of the writ of error for want of jurisdiction. In support of this action Mr. Justice McReynolds observed:

> "Since *Houck* v. *Little River Drainage District,* (1915), 239 U. S. 254, the doctrine has been definitely settled that in the absence of flagrant abuse or purely arbitrary action a state may establish drainage districts and tax lands therein for local improvements, and that none of such lands may escape liability solely because they will not receive direct benefits. The allegations of the original complaint are wholly insufficient to raise the issue in respect of arbitrary legislative action presented by *Myles Salt Co.* v. *Board of Commissioners,* 239 U. S. 478."[67]

The unsuccessful resistant in *Choctaw, O. & G. R. Co.* v. *Mackey*[68] was a railroad assessed for a street improvement. It claimed immunity on the grounds that it was a federal instrumentality for developing Indian coal lands, that the assessment did not sufficiently identify its property, that the statute did not authorize the assessment, that it was not benefited thereby, and that the assessment could be collected only by sale of its property, which would sever an integral part and render it incapable of performing its public duties. No complaint was made of the amount of the assessment in case of liability. Mr. Justice Brandeis answered that if the validity of the assessment was established it might be assumed that due payment would follow, that the fact that the road served the federal government did not render it immune from state taxation, that it was not harmed by any insufficiency in the description of its land which could in no case entitle it to more than a re-assessment, that it was in effect the absolute owner of its road and stations, and that the betterment was of a nature to enhance the value of its use of its facilities, since street paving is a class of betterment to

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[67] A question of whether adequate notice was given in levying a special assessment for the repair of drains is considered in 5 MINN. L. REV. 555.

[68] 256 U. S. —, 41 Sup. Ct. 582 (1921).

which the railroad right of way and stations is generally held to be subject.

In *Kansas City Southern Ry. Co.* v. *Road Improvement District No. 6*[69] an assessment on a railroad for a road improvement was set aside because of the whimsical way in which the alleged benefits were apportioned. Farm lands and town lots were assessed without regard to improvements or to value or to present or prospective use, while the complaining railroad had to pay $7,000 per mile, with the result that it was supposed to be benefited $67,900 for the construction of 11.2 miles of gravel highway. Such an assumption, remarked Mr. Justice McReynolds, "seems wholly improbable, if not impossible," and the assessment was therefore annulled as wholly arbitrary. The statute had set no definite standard for apportioning benefits and the commissioners had not followed consistently any standard of area or location or value. The general principles applicable to special assessments were set forth by Mr. Justice McReynolds as follows:

> "The settled general rule is that a state legislature 'may create taxing districts to meet the expenses of local improvements and may fix the basis of taxation without encountering the Fourteenth Amendment, unless its action is palpably arbitrary or a plain abuse.' * * * Ordinarily, the levy may be upon lands specially benefited according to value, position, area, or the foot-front rule. * * * If, however, the statute providing for the tax is 'of such a character that there is no reasonable presumption that substantial justice generally will be done, but the probability is that the parties will be taxed disproportionately to each other and to the benefit conferred, the law cannot stand against the complaint of one so taxed in fact.' "[70]

A combination of taxation and police power was involved in *Nicchia* v. *New York*,[71] which sustained a statute requiring dogs

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[69] 256 U. S. —, 41 Sup. Ct. 604 (1921).

[70] In 19 Mich. L. Rev. 571 is a note on a state decision holding that an island may not be subjected to a special assessment for a highway on the mainland.

[71] 254 U. S. 228, 41 Sup. Ct. 103 (1921).

to be licensed and providing that the fees collected should go to the American Society for the Prevention of Cruelty to Animals. In essence the complaint of the dog owner must have been that this was taxation for a non-public purpose. Mr. Justice McReynolds answered:

> "And when the state in the reasonable conduct of its own affairs chooses to entrust the work incident to such licenses and collection of fees to a corporation created by it for the express purpose of aiding in law enforcement, and in good faith appropriates the funds so collected for payment of expenses fairly incurred and just compensation for the valuable services rendered, there is no infringement of any right guaranteed to the individual by the federal Constitution. Such action does not amount to the taking of one man's property and giving it to another, nor does it deprive dog owners of liberty without due process of law."[72]

Several tax cases which are appropriately classified under the head of intergovernmental relations may have brief mention here. *Marshall* v. *New York*[73] held that the federal courts should recognize a state's prerogative lien for unpaid taxes and instruct a receiver appointed by the federal courts to pay the taxes in preference to the claims of general unsecured creditors. The decision is not referred to any constitutional issue. It was said to be a question of state law alone whether the lien existed, and it was observed that "the fact that the right rests on common law independently of any statute does not, of course, affect the right of enforcement in the federal courts."

Smith v. *Kansas City Title & Trust Co.*[74] sustained the exemp-

[72] Green v. Frazier, 253 U. S. 233, 40 Sup. Ct. 499 (1920), 19 MICH. L. REV. 134, holding that various enterprises inaugurated by North Dakota are public purposes for which taxes may be levied, is discussed in 8 CALIF. L. REV. 425, 34 HARV. L. REV. 207, 212, 7 VA. L. REV. 306, and 30 YALE L. J. 429.

For other questions of public purpose in taxation, see 9 CALIF. L. REV. 431 on free text-books; 19 MICH. L. REV. 747 on a state cement plant; and 6 CORNELL L. Q. 448 and I WIS. L. REV. 125 on a state bonus to world war veterans.

In 19 MICH. L. REV. 871 is a note on a decision holding invalid, because confiscatory, a tax of $300 a month on scalping theatre tickets.

[73] 254 U. S. 380, 41 Sup. Ct. 143 (1920).

[74] 255 U. S. —, 41 Sup. Ct. 243 (1921).

tion from state taxation accorded to the securities of the federal joint-stock land banks and federal land banks by the Act of Congress creating the banks, and declared that any power to tax the banks is dependent upon congressional permission.

Merchants' National Bank of Richmond v. *Richmond*[75] found that Virginia had taxed the stock of national banks at a higher rate than money loaned at interest, and held that this was a violation of the restriction accompanying the congressional permission to tax the stock—*i. e.*, that the tax "shall not be at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of the state."

Columbia University. THOMAS REED POWELL.

(*To be continued*)

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[75] 256 U. S. —, 41 Sup. Ct. 619 (1921).